



8011-01

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-84517; File No. SR-NYSEArca-2018-54]

Self-Regulatory Organizations; NYSE Arca, Inc.; Order Instituting Proceedings to Determine Whether to Approve or Disapprove a Proposed Rule Change to Amend Commentary .01 to NYSE Arca Rule 8.600-E Relating to Certain Generic Listing Standards for Managed Fund Shares

November 1, 2018

I. Introduction

On July 18, 2018, NYSE Arca, Inc. (“Exchange” or “NYSE Arca”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² a proposed rule change to amend certain generic listing standards for Managed Fund Shares. The proposed rule change was published for comment in the Federal Register on August 7, 2018.³ On September 19, 2018, pursuant to Section 19(b)(2) of the Act,⁴ the Commission designated a longer period within which to approve the proposed rule change, disapprove the proposed rule change, or institute proceedings to determine whether to approve or disapprove the proposed rule change.⁵ The Commission has received no comment letters on the proposed rule change. This order institutes

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 83759 (August 1, 2018), 83 FR 38753 (“Notice”).

⁴ 15 U.S.C. 78s(b)(2).

⁵ See Securities Exchange Act Release No. 84195, 83 FR 48474 (September 25, 2018). The Commission designated November 5, 2018 as the date by which the Commission shall approve the proposed rule change, disapprove the proposed rule change, or institute proceedings to determine whether to approve or disapprove the proposed rule change.

proceedings pursuant to Section 19(b)(2)(B) of the Act⁶ to determine whether to approve or disapprove the proposed rule change.

II. Description of the Proposed Rule Change⁷

Commentary .01 to NYSE Arca Rule 8.600-E sets forth the generic listing standards for Managed Fund Shares. The Exchange proposes to amend Commentaries .01(a) and (b) to NYSE Arca Rule 8.600-E as described below.

A. Proposed Amendments to Commentary .01(a) to NYSE Arca Rule 8.600-E

Commentary .01(a) to NYSE Arca Rule 8.600-E sets forth the generic listing standards applicable to equity securities⁸ in the portfolio of a series of Managed Fund Shares.

1. Proposed Amendments to Commentary .01(a)(2) to NYSE Arca Rule 8.600-E

Commentary .01(a)(2) to NYSE Arca Rule 8.600-E sets forth the generic listing standards applicable to Non-U.S. Component Stocks⁹ in the portfolio of a series of Managed Fund Shares. Commentary .01(a)(2)(A) currently provides that Non-U.S. Component Stocks each shall have a minimum market value of at least \$100 million. The Exchange proposes to amend Commentary .01(a)(2)(A) to provide that Non-U.S. Component Stocks “that in the

⁶ 15 U.S.C. 78s(b)(2)(B).

⁷ For a full description of the proposed rule change, see Notice, supra note 3.

⁸ Commentary .01(a) to NYSE Arca Rule 8.600-E provides that equity securities include the following: U.S. Component Stocks (as described in NYSE Arca Rule 5.2-E(j)(3)); Non-U.S. Component Stocks (as described in NYSE Arca Rule 5.2-E(j)(3)); Derivative Securities Products (i.e., Investment Company Units and securities described in Section 2 of NYSE Arca Rule 8-E); and Index-Linked Securities that qualify for Exchange listing and trading under NYSE Arca Rule 5.2-E(j)(6).

⁹ NYSE Arca Rule 5.2-E(j)(3) defines Non-U.S. Component Stock to mean an equity security that is not registered under Sections 12(b) or 12(g) of the Act and that is issued by an entity that (a) is not organized, domiciled or incorporated in the United States, and (b) is an operating company (including Real Estate Investment Trusts and income trusts, but excluding investment trusts, unit trusts, mutual funds, and derivatives).

aggregate account for at least 90% of the weight of the Non-U.S. Component Stocks of the equity portion of a portfolio” each shall have a minimum market value of at least \$100 million. Commentary .01(a)(2)(B) currently provides that Non-U.S. Component Stocks each shall have a minimum global monthly trading volume of 250,000 shares, or minimum global notional volume traded per month of \$25,000,000, averaged over the last six months. The Exchange proposes to amend Commentary .01(a)(2)(B) to provide that Non-U.S. Component Stocks “that in the aggregate account for at least 70% of the weight of the Non-U.S. Component Stocks of the equity portion of a portfolio” each shall have a minimum global monthly trading volume of 250,000 shares, or minimum global notional volume traded per month of \$25,000,000, averaged over the last six months.

2. Proposed New Commentary .01(a)(3) to NYSE Arca Rule 8.600-E

The Exchange proposes to add new Commentary .01(a)(3) to NYSE Arca Rule 8.600-E, which would provide that the portfolio of a series of Managed Fund Shares may include non-exchange-traded open-end management investment company securities,¹⁰ and such securities would be excluded from the equity portion of the portfolio for purposes of meeting the criteria in Commentary .01(a)(1).

B. Proposed Amendment to Commentary .01(b)(5) to NYSE Arca Rule 8.600-E

Commentary .01(b) to NYSE Arca Rule 8.600-E sets forth the generic listing standards applicable to fixed income securities¹¹ in the portfolio of a series of Managed Fund Shares.

¹⁰ For purposes of proposed Commentary .01(a)(3), non-exchange-traded open-end management investment company securities would not include money market funds, which the Exchange states are cash equivalents under Commentary .01(c) to NYSE Arca Rule 8.600-E and for which there is no limitation in the percentage of the portfolio invested in such securities. See Notice, *supra* note 3, at 38754.

¹¹ Commentary .01(b) to NYSE Arca Rule 8.600-E provides that fixed income securities are debt securities that are notes, bonds, debentures or evidence of indebtedness that include,

Commentary .01(b)(5) currently provides that non-agency, non-GSE and privately-issued mortgage-related and other asset-backed securities components of a portfolio shall not account, in the aggregate, for more than 20% of the weight of the fixed income portion of the portfolio. The Exchange proposes to amend Commentary .01(b)(5) by deleting the reference to the “fixed income portion” of the portfolio, such that non-agency, non-GSE and privately-issued mortgage-related and other asset-backed securities components of a portfolio could not account, in the aggregate, for more than 20% of the weight of the whole portfolio.

III. Proceedings to Determine Whether to Approve or Disapprove SR-NYSEArca-2018-54 and Grounds for Disapproval Under Consideration

The Commission is instituting proceedings pursuant to Section 19(b)(2)(B) of the Act¹² to determine whether the proposed rule change should be approved or disapproved. Institution of proceedings is appropriate at this time in view of the legal and policy issues raised by the proposal. Institution of proceedings does not indicate that the Commission has reached any conclusions with respect to any of the issues involved. Rather, as described below, the Commission seeks and encourages interested persons to provide comments on the proposed rule change.

Pursuant to Section 19(b)(2)(B) of the Act,¹³ the Commission is providing notice of the grounds for disapproval under consideration. The Commission is instituting proceedings to

but are not limited to, U.S. Department of Treasury securities, government-sponsored entity (“GSE”) securities, municipal securities, trust preferred securities, supranational debt and debt of a foreign country or a subdivision thereof, investment grade and high yield corporate debt, bank loans, mortgage and asset backed securities, and commercial paper.

¹² 15 U.S.C. 78s(b)(2)(B).

¹³ Id.

allow for additional analysis of the proposal's consistency with Section 6(b)(5) of the Act,¹⁴ which requires, among other things, that the rules of a national securities exchange be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and to protect investors and the public interest.

The Commission asks that commenters address the sufficiency of the Exchange's statements in support of the proposal, which are set forth in the Notice,¹⁵ in addition to any other comments they may wish to submit about the proposal. In particular, the Commission seeks comment regarding whether the proposal would result in the listing and trading of Managed Fund Shares that are susceptible to manipulation.

As discussed above, the Exchange proposes to amend Commentary .01(a)(2)(A) to NYSE Arca Rule 8.600-E to apply the minimum market value requirement to 90% (rather than 100%) of the weight of the Non-U.S. Component Stocks of the equity portion of the portfolio. The Exchange also proposes to amend Commentary .01(a)(2)(B) to apply the trading volume (shares and notional volume) requirement to 70% (rather than 100%) of the weight of the Non-U.S. Component Stocks of the equity portion of the portfolio.¹⁶ The Exchange states that these amended provisions would be comparable to the current numerical requirements in Commentaries .01(a)(B)(1) and (2) to NYSE Arca Rule 5.2-E(j)(3), which apply to component stocks of an index or portfolio underlying a series of Investment Company Units.¹⁷ The Exchange also states that, like the requirements applicable to Investment Company Units, a

¹⁴ 15 U.S.C. 78f(b)(5).

¹⁵ See supra note 3.

¹⁶ According to the Exchange, these proposals would provide additional flexibility to Managed Fund Shares investing in Non-U.S. Component Stocks. See Notice, supra note 3, at 38754.

¹⁷ See id. at 38753.

substantial portion of the Non-U.S. Component Stocks in the Managed Fund Shares portfolio would be subject to the minimum liquidity and market value requirements.¹⁸ The Exchange additionally states that Non-U.S. Component Stocks would continue to be subject to the weighting and diversification requirements under Commentaries .01(a)(2)(C) and (D) to NYSE Arca Rule 8.600-E.¹⁹

The Commission seeks comment regarding the sufficiency of the Exchange's statements in support of these aspects of the proposal. The Commission also notes that while the proposed numerical percentage thresholds (i.e., 90% and 70%) would be the same as those in Commentaries .01(a)(B)(1) and (2) to NYSE Arca Rule 5.2-E(j)(3), the proposed numerical percentage thresholds would be applied differently from those in Commentaries .01(a)(B)(1) and (2) to NYSE Arca Rule 5.2-E(j)(3). Specifically, the proposal would measure the Non-U.S. Component Stocks that meet the specified quantitative listing standards as a percentage of the Non-U.S. Component Stocks portion of the portfolio. However, Commentaries .01(a)(B)(1) and (2) to NYSE Arca Rule 5.2-E(j)(3) measure the component stocks that meet the specified

¹⁸ See id. at 38753-54.

¹⁹ See id. at 38754. Commentary .01(a)(2)(C) requires that the most heavily weighted Non-U.S. Component stock not exceed 25% of the equity weight of the portfolio and, to the extent applicable, the five most heavily weighted Non-U.S. Component Stocks not exceed 60% of the equity weight of the portfolio. Commentary .01(a)(2)(D) requires that, where the equity portion of the portfolio includes Non-U.S. Component Stocks, the equity portion of the portfolio include a minimum of 20 component stocks; provided, however, that there shall be no minimum number of component stocks if (i) one or more series of Derivative Securities Products or Index-Linked Securities constitute, at least in part, components underlying a series of Managed Fund Shares, or (ii) one or more series of Derivative Securities Products or Index-Linked Securities account for 100% of the equity weight of the portfolio of a series of Managed Fund Shares.

quantitative listing standards as a percentage of the U.S. and Non-U.S. Component Stocks portions of the index or portfolio.²⁰

As discussed above, the Exchange proposes to add new Commentary .01(a)(3) to NYSE Arca Rule 8.600-E to permit Managed Fund Shares to hold non-exchange-traded open-end management investment company securities, and to exclude these securities from the equity portion of the portfolio for purposes of meeting the criteria in Commentary .01(a)(1).²¹ The Exchange argues that, because these securities must satisfy the applicable Investment Company Act of 1940 (“1940 Act”) diversification requirements, and have a net asset value based on the value of securities and financial instruments the investment company holds, it is both unnecessary and inappropriate to apply to such investment company securities the criteria in Commentary .01(a)(1).²² The Exchange also asserts that it would be difficult or impossible to apply to mutual fund shares certain of the generic quantitative criteria in Commentaries .01(a)(1)(A) through (D).²³ Moreover, the Exchange states that Commentaries .01(a)(1)(A)

²⁰ Derivative Securities Products are excluded from Commentaries .01(a)(B)(1) and (2) to NYSE Arca Rule 5.2-E(j)(3).

²¹ According to the Exchange, these securities may be utilized, for example, to obtain income on short-term cash balances while awaiting attractive investment opportunities, to provide liquidity in preparation for anticipated redemptions, or for defensive purposes. See Notice, supra note 3, at 38754. The Exchange states that these securities may include mutual funds that invest principally in securities and financial instruments that help the fund meet its investment objective or equitize cash in the short term. See id.

²² See id. The Exchange also notes that the Commission has previously approved the listing and trading of series of Managed Fund Shares that may invest in non-exchange-traded investment company securities to the extent permitted by Section 12(d)(1) of the 1940 Act and the rules thereunder. See id.

²³ See id. at 38755. The Exchange states that, for example, the requirements in Commentary .01(a)(1)(B) that there be minimum monthly trading volume of 250,000 shares, or minimum notional volume traded per month of \$25,000,000, averaged over the last six months, are tailored to exchange-traded securities and not to mutual fund shares, which do not trade in the secondary market and for which no such volume information is reported. See id. The Exchange also states that it would not be appropriate to apply

through (D) exclude certain “Derivative Securities Products” that are exchange-traded investment company securities.²⁴

The Commission seeks comment regarding the sufficiency of the Exchange’s statements in support of this aspect of the proposal. The Commission notes that, as proposed, the portfolios of generically-listed Managed Fund Shares could be composed of non-exchange-traded open-end managed investment company securities that do not meet the listing standards under Commentary .01(a)(1).²⁵ In addition, as proposed, non-exchange-traded open-end management investment company securities would not include money market funds, which the Exchange states are cash equivalents under Commentary .01(c) to NYSE Arca Rule 8.600-E. However, the Commission notes that “cash equivalents” is defined under Commentary .01(c) to include short-term instruments “with maturities of less than 3 months.” Moreover, while there are currently exceptions for Derivative Securities Products under Commentaries .01(a)(1)(A) through (D), unlike non-exchange-traded open-end management investment company securities, Derivative Securities Products are listed on U.S. national securities exchanges.²⁶

Finally, as discussed above, the Exchange proposes to amend Commentary .01(b)(5) to NYSE Arca Rule 8.600-E to permit portfolios of Managed Fund Shares to potentially hold more non-agency, non-GSE and privately-issued mortgage-related and other asset-backed securities

Commentaries .01(a)(1)(A), (C), and (D) to open-end management investment company securities, and that open-end investment companies hold multiple individual securities as disclosed publicly in accordance with the 1940 Act. See id.

²⁴ The Exchange states that “Derivative Securities Products” includes Investment Company Units, Portfolio Depositary Receipts, and Managed Fund Shares. See id. at 38754.

²⁵ These include, for example, requirements for minimum market value, minimum monthly trading volume, minimum notional volume traded per month, and diversification.

²⁶ See Commentary .01(a) to NYSE Arca Rule 8.600-E (defining Derivative Securities Products to mean Investment Company Units and securities described in Section 2 of NYSE Arca Rule 8-E).

(i.e., no more than 20% of the weight of the whole portfolio) than is currently permitted (i.e., no more than 20% of the weight of the fixed income portion of the portfolio).²⁷ The Exchange states that such investments would be subject to the liquidity procedures adopted by a fund's board of directors.²⁸ The Commission seeks comment regarding the sufficiency of the Exchange's statements in support to this aspect of the proposal.

IV. Procedure: Request for Written Comments

The Commission requests that interested persons provide written submissions of their views, data, and arguments with respect to the issues identified above, as well as any other concerns they may have with the proposal. In particular, the Commission invites the written views of interested persons concerning whether the proposed rule change is consistent with Section 6(b)(5) or any other provision of the Act, or the rules and regulations thereunder.

Although there do not appear to be any issues relevant to approval or disapproval that would be facilitated by an oral presentation of views, data, and arguments, the Commission will consider, pursuant to Rule 19b-4 under the Act,²⁹ any request for an opportunity to make an oral presentation.³⁰

²⁷ The Exchange states that these investments could provide a fund with increased diversification because they may be less correlated to interest rates than many other fixed income securities. See Notice, supra note 3, at 38754.

²⁸ See id. The Exchange also states that the Commission has previously approved the listing of actively managed exchange-traded funds that can invest 20% of their total assets in non-U.S. Government, non-agency, non-GSE and other privately issued asset-backed and mortgage-backed securities. See id.

²⁹ 17 CFR 240.19b-4.

³⁰ Section 19(b)(2) of the Act, as amended by the Securities Acts Amendments of 1975, Pub. L. 94-29 (June 4, 1975), grants the Commission flexibility to determine what type of proceeding – either oral or notice and opportunity for written comments – is appropriate for consideration of a particular proposal by a self-regulatory organization. See Securities Acts Amendments of 1975, Senate Comm. on Banking, Housing & Urban Affairs, S. Rep. No. 75, 94th Cong., 1st Sess. 30 (1975).

Interested persons are invited to submit written data, views, and arguments regarding whether the proposal should be approved or disapproved by [insert date 21 days from publication in the Federal Register]. Any person who wishes to file a rebuttal to any other person's submission must file that rebuttal by [insert date 35 days from publication in the Federal Register].

Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-NYSEArca-2018-54 on the subject line.

Paper comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-NYSEArca-2018-54. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549 on official business days between the hours of 10:00 a.m.

and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-NYSEArca-2018-54 and should be submitted by [INSERT DATE 21 DAYS AFTER DATE OF PUBLICATION IN THE *FEDERAL REGISTER*]. Rebuttal comments should be submitted by [INSERT DATE 35 DAYS AFTER DATE OF PUBLICATION IN THE *FEDERAL REGISTER*].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.³¹

Eduardo A. Aleman,
Assistant Secretary.

³¹ 17 CFR 200.30-3(a)(57).

